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IN THE

Supreme Court of the United States

October Term, 1965.

No. 1253

WILLIAM S. and MARY P. SERRI,
Petitioners,

against

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

To the Honorable the Chief Justice and the Associate Justices of the United States:

Petitioners, William S. and Mary P. Serri, pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in the above-entitled case on December 2, 1965.

CITATIONS TO OPINIONS BELOW.

The memorandum opinion of the Tax Court is not officially reported and is printed (R 121a-160a) in the Appendix to Brief for Petitioners, which was filed with the court below. The per curiam opinion of the Court of Appeals for the Third Circuit printed in Appendix B hereto, *infra*, p. 30, is reported at 354 F. 2d 1002.

JURISDICTION.

The judgment of the Court of Appeals was entered on December 2, 1965. A duly filed Petition for Rehearing was denied on February 18, 1966. The jurisdiction of this Court is invoked under 28 U. S. C. Section 1254(1) and 26 U. S. C. Section 7482(a).

QUESTIONS PRESENTED.

The Court of Appeals has issued a per curiam affirmance of the Tax Court's finding, based upon a reconstruction of income under the net worth method, that taxpayers fraudulently underpaid their income tax for each of the years 1947 and 1949-1956, inclusive. The questions presented are:

1. Is not the per curiam affirmance of the Tax Court's holding that it is only necessary for the Commissioner to negate the taxpayers' assertion of a family cash accumulation by a preponderance of the evidence in direct conflict with the decided cases of the Court of Appeals for the Fifth Circuit which holds that the Commissioner has the burden of proving all the elements of a net worth case by clear and convincing evidence?

2. Is not the per curiam affirmance of the Tax Court's requirement that taxpayers must prove the exact amount of cash received, after having established that some cash was turned over to husband-taxpayer as custodian following his father's death in 1944, in direct conflict with the decided cases of the Court of Appeals for the First and Sixth Circuits which hold that once the Commissioner's determination of cash is found to be wrong, then it is not incumbent on the taxpayers to establish the amount of cash on hand as of a given date?

3. Are this Court's decisions in *Holland v. United States*, 348 U. S. 121 (1954) (that the Commissioner must establish a likely source of currently taxable income) and *United States v. Massei*, 355 U. S. 595 (1958) (that, in lieu of establishing a likely source of taxable income, the Commissioner need only negate all possible sources of nontaxable income) mutually exclusive, so that the Commis-

sioner, in order to prove fraud by clear and convincing evidence, need only negate the sole source of non-taxable receipts claimed by the taxpayers, even though, in the process of presenting his case, his witnesses have established that taxpayers did not have a likely source of taxable income which could give rise to income in excess of that reported on their income tax returns?

4. Is not the per curiam affirmance of the Tax Court decision a sanctioning of such a departure from the accepted and usual course of judicial proceeding as to call for an exercise of this Court's power of supervision in light of the fact that the Tax Court

(a) arbitrarily disregarded competent, relevant, credible and uncontradicted testimony of the Commissioner's six witnesses which, if accepted, would have established taxpayers' innocence,

(b) misled taxpayers' counsel as to the Court's acceptance of the credibility of this testimony and thereby caused counsel to refrain from presenting substantial additional proof to corroborate this testimony,

(c) arbitrarily denied counsel the opportunity to call additional witnesses in order to overcome the Court's belated rejection of the earlier testimony,

(d) arbitrarily ignored the fact that the Commissioner could not produce one patient who paid taxpayer more money than taxpayer indicated he had received per a patient study which listed all visits by named patients over a five-year period and which was given to the Commissioner five years prior to trial, and

(e) misconstrued the evidence necessary to sustain a finding of fraud?

5. Are not such departures from the accepted and usual course of judicial proceeding so egregiously erroneous as to constitute a denial of due process?

STATUTES INVOLVED.

The statutory provisions involved are Section 1112 of the Internal Revenue Code of 1939, 53 Stat. 160, 26 U. S. C. 1955 Ed. § 1112, and Section 7454(a) of the Internal Revenue Code of 1954, 68A Stat. 884, 26 U. S. C. 1955 Ed. § 7454(a). These provisions are printed in Appendix A, *infra*, p. 29.

STATEMENT.

The jurisdiction of the Tax Court was invoked following the Commissioner's issuance of his ninety-day letter, wherein he reconstructed taxpayers' income by using the net worth method and charged that they had fraudulently evaded income taxes. The Tax Court found taxpayers liable for deficiencies in income taxes for the years 1947 and 1949 to 1956, inclusive, of $123,051.97 and additions to the tax of $67,563.04, being the 50 per cent fraud penalty and the underestimation of estimated tax penalty. A Petition for Review by the Court of Appeals for the Third Circuit was duly filed and that Court, stating that it found no error, affirmed the Tax Court per curiam. A duly filed Petition for Rehearing was denied on February 18, 1966.

The necessary facts to support this petition are taken from the Tax Court's memorandum findings of fact and opinion and from the undisputed evidence developed throughout the proceeding below.

Taxpayers are husband and wife who reside in Merchantville, New Jersey, and filed their returns with the proper official of the Internal Revenue Service at Camden, New Jersey, during all the years in question (R 123a). Husband-taxpayer (hereinafter referred to as "taxpayer") is a medical doctor engaged in general practice, with offices in Camden, and Swedesboro, New Jersey, during each of the years involved (R 124a).

It was stipulated that taxpayer worked 275 full days a year (R 126a). The Tax Court found that taxpayer worked 14 hours per day (R 126a). Not all of this time was devoted to treating patients (R 82a-83a, 97a-100a, 111a-113a). As a result of a mathematical application of the Tax Court's findings, it is seen that the Court concluded that taxpayer treated patients for 13 hours a day (brief, *infra*, pp. 19-20).

Taxpayer had a standard procedure which he followed in treating patients. A patient would enter his office, remove his outer garments and be weighed (R 10a, 17a, 20a, 23a, 24a, 85a-86a, 100a-101a, 112a). The patient would then be seated next to taxpayer at his desk while his assistant, Miss Jeannette Kanady, would obtain and give to taxpayer the patient card record on which he entered the patient's name, address and medical history (R 10a, 17a, 20a, 86a, 101a, 127a). Taxpayer would spend some time in "small talk" in order to relax the patient so that his blood pressure might be properly read and his chest listened to (R 10a, 17a, 20a, 23a, 24a, 86a, 101a, 112a). The examination proper would then take place. Taxpayer would inquire as to the nature of the illness, make his diagnosis, treat the patient and give him any necessary injections and heat therapy (R 13a, 19a, 23a, 101a). The examination would take as long as necessary since taxpayer was a painstaking doctor who never rushed his patients (R 10a, 12a, 14a, 17a, 20a, 22a-23a, 24a, 37a, 86a, 112a). Upon completion, the patient's medical record card would be updated and Miss Kanady would be instructed as to the medications to be supplied to the patient (R 10a, 101a). She would place these in envelopes and taxpayer would write his instructions on the envelopes (R 101a). On each occasion the patient was given several packets of pills (R 11a, 13a, 16a-17a, 19a-20a, 23a, 125a). The patient would then dress and leave (R 101a).

After testifying about the above procedure, the six patients that the Commissioner called as his witnesses esti-

mated that they spent from a few minutes to forty-five minutes with taxpayer on each visit, with the normal visit being fifteen minutes (R 11a-12a, 13a, 18a, 20a, 23a, 25a). At the trial, the Tax Court indicated its acceptance of the accuracy of the six patients' testimony (R 42a). However, in its opinion, issued 19 months later, the Tax Court said it did not believe that the patients had testified accurately, and, therefore, concluded that taxpayer spent less than nine minutes with a patient (R 125a, 147a-148a).

Taxpayer charged each patient the same fee for each visit unless it was an unusual situation. The normal fee was stipulated to be the average fee for the following years in question: $3.00 in 1951 and 1952, $3.50 in 1953 and 1954, and $4.00 in 1955 (R 125a).

On January 5, 1942, taxpayers filed a financial statement with the Nutter Mortgage Service Company, Camden, New Jersey, which did not list as an asset any cash on hand in excess of $12,000 (R 134a). As of that date, taxpayer's father, Salvatore Serri, was living, and was custodian of the family savings which arose from the earnings of Salvatore Serri, his wife, Maria, his mother, Carmela, and his two sons, Humbert and William, the aforesaid taxpayer (R 76a-77a). The exact amount of the savings is in dispute, but the Tax Court indicated that there was some cash accumulation (R 136a, 151a).

The Salvatore Serri family had many sources of income. The Tax Court found that the cash generated thereby was placed originally in a steel box and later in a large safe in the family residence, the safe having been purchased in 1926 (R 136a).

In 1944, taxpayer's father died and taxpayer became custodian of the fund (R 76a-77a, 88a, 118a).

In 1949 taxpayer met LeRoy Ireland, an art expert, and sought his assistance in investing in paintings (R 60a). Taxpayer told Ireland in 1949 that he had $125,000 of the Salvatore Serri family money to invest in art and art objects (R 60a, 61a, 62a).

In 1950 taxpayer met John Walton, an antique dealer, and asked his aid in investing in antiques (R 90a). He told Walton that he had around $100,000 or $125,000 that he wanted to invest in furniture and this money belonged to the Salvatore Serri family (R 90a, 93a, 96a).

On April 18, 1956, Revenue Agent Madden began an audit of taxpayers' 1954 return (R 43a). Special Agent McElroy began his investigation on January 24, 1957 (R 25a). The agents concluded that taxpayer's books and records were inadequate since taxpayer's expenditures exceeded the income reflected on his returns (R 26a, 44a-45a). This resulted in the agents employing the net worth method of computing income (R 44a-45a).

Taxpayer's expenditures exceeded the income reflected on the tax return because he was purchasing paintings and antiques during the years in question (R 26a, 44a-45a). It was stipulated that taxpayer purchased $246,242.58 of such art objects during the period (R 130a-131a). It was not stipulated on whose behalf taxpayer purchased the art objects or with whose funds (R 4a-5a, 130a-131a). Taxpayer contends that the art objects were purchased by him as custodian when he invested the Salvatore Serri family funds. The Commissioner and the Tax Court concluded that taxpayer personally acquired the items out of his taxable income. The Tax Court found that during the period taxpayer failed to report $240,090.05 of income from his medical practice (R 142a-143a, as adjusted by 130a). It was stipulated that the Commissioner was not alleging any concealed source of income or that the income was derived from any illegal activity (Appendix C, *infra*, p. 34).

To assist Agents Madden and McElroy in their examination, taxpayer had his accountant analyze the patients' card records for the years 1951 to 1955 (R 27a). The card study listed the names and addresses of the patients and the number of visits each patient made by month and year (R 27a). There were approximately 5000 different pa-

tients' names listed in the card study (R 116a-117a, 118a). Taxpayer requested that the agents verify the accuracy of the card study by actual patient interviews (R 28a). It was taxpayer's purpose to have the agents verify the patient visits and multiply those visits by his set fees (*i.e.*, the ones that were later stipulated to in open court), and this resulting figure would fully support the medical receipts set forth on the filed tax returns (R 45a-47a). The card study was given to the agents in 1958, some five years prior to the trial, and they kept it as long as they desired (R 29a-30a). The agents investigated the card study and the Commissioner relied on it to select the witnesses that he called at the trial (R 120a).

On March 10, 1959, a criminal indictment was filed charging taxpayer with willful attempted evasion of income tax (R 141a). On December 22, 1959, due to his physical condition and his need to fulfill his commitments to patients under his continuing care, taxpayer, on advice of counsel, pleaded *nolo contendere* to one count of the indictment that pertained to 1954 (R 106a). Taxpayer properly understood that such a plea was not determinative in the civil action and at that time he could present his defense (R 106a). On March 4, 1960, he was fined $10,000.00 and placed on probation for five years (R 141a-142a).

On January 18, 1961, Commissioner issued his ninety-day letter. Short of proving fraud, the statute of limitations barred any assessment for years prior to 1954. Short of either proving fraud or the omission of 25 per cent of gross receipts, the statute of limitations barred any assessment for the years 1954 and 1955. The year 1956 was open. The case was tried in January 1963, before Judge Hoyt of the Tax Court. Nineteen months later, on August 18, 1964, the opinion was handed down which sustained the Commissioner's asserted deficiencies and penalties for 1947 and 1949 to 1956, inclusive.

On September 16, 1964, taxpayers filed a motion requesting a rehearing on the basis that taxpayers could not reasonably be expected to foresee that Judge Hoyt would reject the uncontradicted testimony of the Commissioner's witnesses that was favorable to taxpayers, *i.e.*, the length of time that the patients spent with taxpayer on an average visit. Taxpayers' motion requested a further hearing in order to take the testimony of as many patients as Judge Hoyt would personally select from a list of 500 or more patients in order to establish to his satisfaction that the Commissioner's patient witnesses correctly stated the facts. This motion was denied.

Decision was entered under Rule 50 on December 1, 1964. A petition for review by the Court of Appeals for the Third Circuit was filed February 26, 1965. That Court affirmed the decision on December 2, 1965, and denied a petition for rehearing on February 18, 1966.

REASONS FOR GRANTING THE WRIT.

I.

The Decision of the Court Below Conflicts With Applicable Decisions of Other Circuit Courts.

A. Conflicting Requirements Concerning the Degree of Proof Needed for Elements of a Net Worth Case.

By statute, see Appendix A, the burden of proving fraud is on the Commissioner. By case law, the burden can only be met with clear and convincing evidence. *Valetti v. Commissioner,* 260 F. 2d 185, 188 (CA 3, 1958). The Commissioner must prove every fact relied upon to support the ultimate conclusion of fraud.

> "*Since the burden was on the Commissioner to prove fraud, it must follow that he had the burden of proving every subsidiary fact relied upon by the court to support that ultimate conclusion.* To permit, in satisfying this burden, the use of a Commissioner's finding that was to be accepted only because the taxpayer had failed to meet a burden of overcoming it, would be to allow the Commissioner to raise himself by his own bootstraps. . . ." (Emphasis added.) *George v. Commissioner,* 338 F. 2d 221, 223 (CA 1, 1964).

The heart of this case is whether or not taxpayer's taxable income from his medical practice for the years 1947 and 1949 to 1956, inclusive, could generate $240,090.05 of unreported income (Appendix C, *infra,* p. 31, Chart A) over and above the $408,263.06 reported on his returns (Appendix C, *infra,* p. 31, Chart B). It was stipulated that the Commissioner was not alleging any concealed source of income or that the income was derived from any illegal activity (Appendix C, *infra,* p. 34). Taxpayer's

position was that he could not earn such a sum and that the so-called unreported income was actually funds that he spent as custodian for the Salvatore Serri family. The Commissioner denied the existence of this cash accumulation. The Tax Court agreed with the Commissioner and stated:

> ". . . Based on the entire record, we hold also that the respondent has *proved by a preponderance of the evidence* that this alleged cash hoard was not the source of petitioner's net worth increases over the years." (Emphasis added.) (R 157a)

The Third Circuit's per curiam affirmance of the fact that the cash fund can be negated by a mere preponderance of the evidence is in direct conflict with the Fifth Circuit which properly applied the safeguards announced by this Court in *Holland* when that Circuit held:

> ". . . To prove fraud, however, the Government was bound to establish *by clear and convincing evidence that such increases as were reflected by its computations, represented then current, taxable income, and by the same degree of proof to show that these increases were not attributable from amounts earned in prior years as was claimed by the taxpayer.* Holland v. United States, 348 U. S. 121, 75 S. Ct. 127, 99 L. Ed. 150. The Government did neither." (Additional emphasis added.) *Fairchild v. United States,* 240 F. 2d 944, 947 (CA 5, 1957).

As the matter now stands, the Third Circuit has unequivocally approved the Tax Court's downgrading of the burden of proof required to establish fraud. This represents a patent erosion of the *Holland* safeguards. Unless this Court takes jurisdiction, as requested herein, it is reasonable to expect that the case of *William S. Serri,* 23 TCM 1319 (1964), aff'd. 354 F. 2d 1002 (CA 3, 1965), cert. den. — U. S. — (1966) will be cited by Government

counsel more frequently than any other net worth case—including *Holland*—as the Commissioner uses *Serri* as a battering ram to destroy the remaining protection given taxpayers by this Court.

This is the most important net worth decision since *Holland*. It directly affects every future net worth case. It is respectfully suggested that this Court should grant the writ in order to correct the error in this case and to protect the rights of future taxpayers. This conflict can only be effectively resolved by the prompt action of this Court.

B. Conflicting Requirements Concerning Proof of Exact Amount of Cash Accumulation.

This Court stated in *Holland v. United States*, 348 U. S. 121, 132 (1954) that the Commissioner had to establish all of the assets in an opening net worth statement with reasonable certainty. It follows that each year's net worth statement must be established with the same certainty, if valid comparisons are to be made. The parties stipulated the amount of cash in bank for the various years (R 132a-133a). There was no stipulation as to cash on hand, but the Commissioner credited the taxpayers with $4,000 cash on hand in the opening net worth statement for 1942 and in each subsequent one (R 147a). The Tax Court accepted the Commissioner's determination that cash on hand was a constant $4,000 from 1942 to 1956.[1]

Despite this finding, *The Tax Court concedes that taxpayer, following his father's death in 1944, received some*

1. The final figures used by the Commissioner in his deficiency determination (R 142a-143a) were adopted by the Tax Court with the exception of an inheritance of $5000 and a related bank account (R 130a). Comparing these figures with the total assets listed at R 132a-133a, an annual $4000 difference is found in all years except 1955 and 1956. In those two years, the Commissioner added $1000 for the disputed bank account (R 130a) and $12,100 for a disputed antique purchase (R 131a). After eliminating these two items, the difference is exactly $4000 in 1955 and 1956.

cash as custodian. The Court specifically found (R 136a) that the Salvatore Serri family funds were placed in a steel box up until 1926, and then a large safe was purchased to house the fund. The Tax Court had no doubt about this, but it did doubt that the fund was a "large" or "substantial" one.

> "The Serri family did not accumulate a *large* cash hoard during the life of Salvatore Serri. . . ." (Emphasis added.) (R 144a)
>
> "We are unable to believe Serri's claims that his family had accumulated a *large* hoard of money which they kept originally in a steel box but transferred to the safe in 1926 and which he later placed in safe deposit boxes of his own. . . ." (Emphasis added.) R 149a)
>
> "Perhaps *some cash* was turned over to Serri by his mother after her husband's death. He was the elder son and the male head of the Serri family. *We cannot speculate, however, about that.* Other than the diary entry, which we reject, there is no evidence of a count or even of an estimate of the size of the fund in 1944. On the evidence before us we can only conclude *that no large family cash* fund existed or was used by Serri to purchase over $250,000 worth of antiques and art objects in the period from 1949 to 1956. Neither the diary entry nor all of the evidence offered persuade us that we should so conclude." (Emphasis added.) (R 151a-152a)
>
> ". . . Consequently, we conclude that Serri never became the custodian of any *substantial* amount of family funds, and the money he spent through the years for art objects and antiques was his own." (Emphasis added.) (R 153a)

However, once it is established that *some* funds were turned over to taxpayer, then the certainty of the net worth calculation falls since it is admittedly inaccurate

because it does not consider *any* cash as coming from that source, but instead treats *all* of it as money from earnings (R. 157a). The Commissioner's determinations are, therefore, arbitrary and excessive.

The Third Circuit's per curiam affirmance of the Tax Court's position (R 151a, 155a) that the taxpayer had to prove how much cash he received as custodian before any error could be admitted in the net worth calculation is in direct conflict with the well-reasoned opinions of the First and Sixth Circuits which held that the Commissioner must make proper allowance for the cash and that his failure to do so must result in a decision for the taxpayer. See *Thomas v. Commissioner*, 232 F. 2d 520, 526 (C. A. 1, 1956); *Thomas v. Commissioner*, 223 F. 2d 83, 88 (CA 6, 1955) (opinion of Justice Stewart) and *Grubb v. Commissioner*, 315 F. 2d 753 (CA 6, 1963) at p. 759, where the Court said:

> *"When the Commissioner's determination is wrong, no presumption of correctness attaches to it, and there is no burden upon the taxpayer to show what is the correct determination.* The Tax Court found that the Commissioner's computation of cash on hand was incorrect. There is no evidence that petitioner had cash on hand (as the Tax Court found) in the amount of $14,965.75 on December 31, 1940, and the same amount of cash on hand at the close of 1941, 1942, 1943, and 1944; and that the amount of cash on hand at the close of 1945 was double the amount of any of the other years. The computations of cash on hand found by the Tax Court are arbitrary and, as far as can be ascertained, based on a guess. Accuracy in the determination of opening net worth is necessary in net worth cases, and accuracy in the determination of cash on hand at the opening of the net worth period is necessary to establish the opening net worth. *Thomas v. Commissioner*, 232 F. 2d 520, 526 (CA 1); *Holland v. United States*, 348 U. S. 121, 132. . . .

"Once the determination of the Commissioner is found to be wrong, it is not incumbent on the taxpayer to prove that he owes no tax, or what tax he did owe.

"After finding that the Commissioner was mistaken in his computations of petitioner's cash on hand, the Tax Court erred in holding that the burden was upon the taxpayer to establish what amounts of cash he had on hand at the end of any of the years 1940-1945." (Additional emphasis added.)

This Court should take jurisdiction in this matter in order (1) to resolve the conflicts that have arisen between the Circuits as to the degree of proof for fraud and to the burden of proving the exact amount of cash, and (2) to reaffirm the safeguards that must be applied to any case established by inferences drawn from a net worth study.

II.

Are the Decisions of This Court in *Holland v. United States* and *United States v. Massei* Mutually Exclusive?

In *Holland v. United States*, 348 U.S. 121 (1954) this Court held that one of the essential elements that the Commissioner had to establish in proving a net worth case was a likely source of currently taxable income. Later, in *United States v. Massei*, 355 U.S. 595 (1958) this Court held that in lieu of establishing a likely source of taxable income, the Commissioner need only negate all possible sources of non-taxable income. The instant case presents a third situation which falls between *Holland* and *Massei* into an area where this Court has not ruled.

The Tax Court relied on *Massei* for the proposition that the Commissioner had fulfilled his requirement of establishing a likely source of taxable income by negating the sole source of non-taxable receipts relied on by the taxpayer, *i.e.*, the family cash accumulation (R 148a). The

Tax Court concluded that there was no significant cash accumulation and found that all of the "unreported income" came from the medical practice (R 157a).

If this was all that the Commissioner did, then, assuming *arguendo,* the Tax Court could decide that the Commissioner had clearly and convincingly established a likely source. The Commissioner, however, went further than this and attempted to show directly that the likely source was taxpayer's medical practice. To this end the Commissioner called six patients of taxpayer as his witnesses (R 6a-25a). Subsequent to their testimony, and as a direct result of it, the parties stipulated (R 45b-46b) that taxpayer worked 275 full days and that his regular set fee for each patient visit was deemed to be the average fee for all visits for 1951-1955, inclusive, thus excluding any variation for free visits and the more expensive home visits and x-ray treatments (R 125a).[2]

With the average fee stipulated, one can calculate the number of patient visits needed to produce the income reported on taxpayers' tax return and the number of additional visits needed to generate the alleged unreported receipts. Charts C and D (Appendix C, *infra,* p. 32) reveal that an average of 13,741 patient visits were reported on the tax returns during the period, while the Commissioner contended that the average was 25,214, or some 11,473 visits over and above that reported by the taxpayer.

Knowing the number of patient visits, the next question becomes how long was the average visit? Once this is known, it can be seen if the Commissioner's determination of the additional unreported visits is realistic.

The six witnesses for the Commissioner testified as follows:

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2. The years 1951-1955 have more facts stipulated about them than any other period because these were the first years to be investigated. This period is most critical since the alleged unreported income of $194,964.08 for this period is over 80 per cent of the total alleged unreported income of $240,090.05. See Appendix C, *infra,* p. 31, Chart A.

Witness	*Statement*
Wickizer	few minutes to half an hour or longer (R 11a)
Stinger	twenty minutes to half an hour (R 13a)
Vernelson	fifteen or twenty minutes (R 18a)
Castle	quarter of an hour or better (R 20a)
Harre	fifteen minutes (R 23a, 24a)
Gravino	fifteen or twenty minutes to three-quarters of an hour or so (R 25a)

The normal visit, therefore, was no less than fifteen minutes or four visits an hour. This means that the taxpayer reported that he worked 3435 hours in an average year (13,741 ÷ 4), while the Commissioner asserted he worked 6303 hours in the average year (25,214 ÷ 4).

The number of days that taxpayer worked was stipulated to be 275 full days (R 45b). Thus, taxpayer treated patients on an average of 12½ hours a day on the basis of his tax returns (3435 ÷ 275) [3] while the Commissioner's figures show that the taxpayer worked 23 hours each and every working day throughout the five-year period (6303 ÷ 275). This is an absurdity since it is physically impossible to work at that sustained pace.

Instead of proving by clear and convincing evidence that the medical practice was the likely source of the "unreported" income, the Commissioner affirmatively showed that it was not the source of any additional income. Since it was stipulated that the Commissioner was not alleging any concealed source of income or that the income was derived from any illegal activity (Appendix C, *infra*, p. 34), then the funds used to purchase the antiques and art objects must have been Salvatore Serri family funds.

3. Note: The Tax Court accepted this result in principle, since it found that taxpayer worked 14 hours a day (R 126a), with this figure including non-patient treating time as well as time spent with patients.

At this point, the Commissioner has shown that there is no likely source as *Holland* requires, but the Tax Court has accepted the discrediting of the family cash on a *preponderance of the evidence* (R 157a) and has sustained the Commissioner's net worth calculation and fraud charge on the principles announced in *Massei*. Clearly, the two situations are not consistent.

This third situation where the Commissioner has (possibly) discredited the non-taxable source, but at the same time has shown that there is no likely source, represents an area wherein this Court has not ruled, but should do so. The Third Circuit's per curiam affirmance of the Tax Court under these circumstances does violence to the safeguards announced by this Court in *Holland,* and is in conflict with that case as a matter of principle since there has been affirmative proof that the medical practice was not the likely source of unreported income and there is no other possible taxable source. It is respectfully urged that this Court take jurisdiction in order to resolve the hiatus between its two earlier opinions.

III.

The Need for an Exercise of This Court's Power of Supervision in Order to Prevent a Denial of Due Process.

A. Disregard of Uncontradicted Testimony by Commissioner's Witnesses.

As previously noted, the Tax Court found that the entire alleged unreported income of $240,090.05 came from taxpayer's medical practice (R 157a). The key issue here, then, is how much could taxpayer earn from his practice. This issue affects not only the fraud charge, but also the question of deficiencies. It should be borne in mind that taxpayer reported $408,263.06 in medical receipts on his tax returns during the years in question (*supra,* p. 10).

The medical receipts of taxpayer can be calculated on an annual basis by applying the following formula:

> Average fee per visit × number of patient visits per hour × number of hours per day spent treating patients × number of days worked per year.

In this formula, it was stipulated (R 125a), that the average fee per patient was $3.00 in 1951 and 1952, $3.50 in 1953 and 1954 and $4.00 in 1955. It was also stipulated (R 126a) that taxpayer worked 275 days a year. Thus, for 1951 to 1955, inclusive, the only missing factors are the number of patient visits per hour and the number of hours per day spent treating patients.

As Chart A (Appendix C, *infra,* p. 31) shows, over 80 per cent of the alleged unreported income is attributable to 1951-1955, inclusive. Thus, this period, in which two of the four factors in the formula are stipulated, is determinative of the entire case.

It has previously been established that the six witnesses of the Commissioner who were also patients of taxpayer testified that the average treatment was fifteen minutes, or four patients an hour. The Tax Court, however, concluded that the correct number was seven per hour (R 125a).[4]

The Tax Court did not make a specific finding as to the number of hours that taxpayer spent in treating patients, but merely found that his work day averaged 14 hours (R 126a). Taxpayer and his assistant testified that he spent approximately two hours a day in medical activity that did not involve patient treatments (R 98a-99a, 111a-

4. Having rejected the uncontradicted testimony of the patients, the Tax Court then (R 148a) states that taxpayer's argument that his medical practice would not support the income attributed to him by the Government is not "essential to a proper determination of the issues presented here" and turns to *Massei* to avoid the problems of a likely source of income. However, the grave limitations on the applicability of *Massei* under the circumstances of this case has been discussed in Section II, *supra.*

112a). The Tax Court apparently modified this testimony to one hour a day for non-patient activity, since calculations made on seven patients an hour for a 13-hour day ($425,425.00) support the Rule 50 computation almost to the penny ($426,931.96). See Appendix C, *infra*, p. 33, Chart E.

Thus, it is apparent that *the Rule 50 computation is only supportable if taxpayer saw seven patients an hour* for 13 hours a day for the stipulated 275 days a year and charged the stipulated fees.

There is absolutely nothing in the record to support the finding that taxpayer saw seven patients an hour. *If the record made by Commissioner's witnesses is adopted ($243,100.00), as it should be, then it reveals that taxpayer reported his income ($231,967.88) in full and paid the proper tax thereon.* See Appendix C, *infra*, p. 33, Chart F.

As Chart F shows, the acceptance of the testimony of Commissioner's witnesses produces figures which exceed reported income by less than $11,200, or less than five per cent over a five-year period. This differential is due to the use of average figures over the period and the fact that taxpayer did not work 13 hours on days he did not have hours in both Swedesboro and Camden. A mere five per cent discrepancy certainly cannot constitute clear and convincing evidence of fraud.

Now the issue is drawn. If the Commissioner's witnesses testified accurately, then the Commissioner has failed to prove fraud by clear and convincing evidence. If the Tax Court is correct in rejecting the witnesses' testimony, then there is a substantial understatement of income which could be the basis for sustaining a finding of fraud.

The Tax Court must do two things in order to sustain its discrediting of the testimony. First, it must give valid reasons as to why it rejected the uncontradicted testimony as being untrustworthy and, second, it must show where the record will support the figure seven that it says is correct. The Tax Court did neither.

A detailed examination of the record shows that the patients' testimony fully developed the painstaking routine that taxpayer employed in examining his patients. This routine is set forth in detail in the statement of the case, but, in summary, every patient was weighed, had his blood pressure checked, removed his outer garments so that his chest could be examined, was examined for the particular ailment that prompted the visit, always received pills with detailed instructions as to their use and injections and heat therapy where necessary. As all of the patients indicated, this was the normal routine and it was with this background that the patients testified to the time they spent with taxpayer.

Furthermore, the revenue agent (R 54a-55a), the special agent (R 37a) and regional counsel (R 57a) all admitted, in open court, that they knew of nothing to contradict this testimony, nor did they even try to refute it. On this record, the Tax Court concluded (R 148a) that taxpayer saw seven patients per hour since all of Commissioner's witnesses' memories had dimmed (R 147a) even though the record shows that four of them (and, in fact, all of them) were still patients of taxpayer at the time of the trial (Wickizer R 6a; Stinger R 13; Castle R 19a; Harre R 23a). *There is nothing, in or out of the record, to support such a finding—yet without it the Commissioner has not and cannot prove his case.*

The Tax Court came to the amazing conclusion that the six witnesses put on by the Commissioner who independently testified to their own personal experience as patients of taxpayer all suffered from faulty memories. *The Tax Court did not conclude that only one witness could not remember. It said every one of the six who testified had the same problem. This is not by any stretch of the imagination a question of the credibility of the witnesses. The testimony of the six witnesses was not attacked by the Commissioner —he even admitted it was consistent with what he had been*

told previously (R 37a) *and that he knew of nothing to contradict their statements.*

> "We recognize the general rule, of course, as stated by both courts below, that the question of the credibility of witnesses is one for the . . . [judge] alone; but this does not mean that the . . . [judge] is at liberty, under the guise of passing upon the credibility of a witness, to disregard his testimony, when from no reasonable point of view is it open to doubt." *Chesapeake & Ohio Ry. v. Martin,* 283 U. S. 209, 216 (1931).

The Tax Court's rejection of the testimony was an arbitrary and unwarranted act and the Third Circuit's affirmance of this disregard of competent, relevant, credible and uncontradicted testimony of the Commissioner's own witnesses in order to sustain a finding against the taxpayer, is in clear violation of the accepted and usual course of judicial proceeding and is tantamount to a denial of due process. See *Duffin v. Lucas,* 55 F. 2d 786, 798 (CA 6, 1932).

There is nothing inherently improbable in the patients' testimony nor is it incredible on its face or as to its substance; therefore, *it must be accepted as establishing the fact that taxpayer treated four patients an hour. Herbert v. Riddell,* 103 F. Supp. 369, 389 (SD Calif. 1952) (Yankwich, J.).

The Tax Court justifies disregarding Commissioner's witnesses' direct testimony as to the length of the patient visit and explains its personal choice of the number seven because:

> "In finding that patients did not spend an average of from 10 to 15 minutes per visit with Serri, we rely upon the fact that it was necessary for Serri to have a numbering system, that the patients found it desirable to come as early as 5:00 in the morning and to sleep in cars or wait until their numbers came up, that Serri's fees were small and uniform, and that he had

at least one full-time and one part-time assistant. All these facts indicate a rather rapid patient turnover. . . ." (R 148a)

It is true that taxpayer's fees were small and uniform and that he had Miss Kanady as a full-time assistant and part-time x-ray assistant who worked two days a week in Camden (R 125a), but these two factors do not contradict or vary in the slightest the direct testimony of the patients that the Commissioner put on the stand. No legitimate inference to the contrary can be drawn.

It is also true that taxpayer used a numbering system for patients, but it was used only in Swedesboro (R 21a), while in Camden the patients had to have appointments (R 7a). The Tax Court's contrary findings of fact (R 125a) is in error.

The numbering system does not indicate a rapid turnover. To the contrary, it indicates a slow turnover. Taxpayer explained (R 78a-79a) that the numbering system was installed so that a patient could get his number and then leave the area to do errands and return shortly before his number would be reached. A telephone call to Miss Kanady enabled the patient to calculate the time he should return (R 78a). This testimony was confirmed by Commissioner's witnesses, Wickizer (R 7a) and Harre (R 21a). Thus, the numbering system indicated a long wait which could only be avoided by taking a number and then doing some other task during the interim until taxpayer could see the patient.

Those who arrived early and slept in cars were those who wanted an early visit (R 79a) since they had other things to do later on in the day and could not return.

Again, there is absolutely nothing in the record to sustain the Tax Court's complete disregard of the direct testimony of knowledgeable witnesses who were Commissioner's witnesses—not those of taxpayer—and its arbitrary selection of the number seven. *Even if the direct testimony could be disregarded the finding that taxpayer*

saw seven patients an hour is sheer speculation. The number seven was never mentioned at the trial. It is totally devoid of evidentiary support and to base a decision on such an unsupported finding is a denial of due process.

B. Taxpayers' Counsel Misled by Statements of Court.

Taxpayers' counsel was misled by the Tax Court during the course of the trial. The Commissioner selected these six witnesses to establish his case. Obviously, he considered their veracity and believed that they testified truthfully and consistently with prior statements (R 37a, 54a-55a, 57a). The Tax Court also noted its acceptance of this testimony without any reservation, when it remarked to Commissioner's counsel during the trial (less than 48 hours after hearing the patients testify):

> "Will this conflict with the testimony from your own witnesses? They all had long visits and spent from 15 to 20 minutes, or up to 45 minutes with the Doctor. They were your witnesses." (R 42a)

Counsel justifiably relied upon the Court's statement at the trial that the judge understood and accepted the length of time of the average visit. Thus, counsel concluded that the length of a visit was not in dispute, there being nothing in the record to contradict the testimony of the Commissioner's witnesses. In order to avoid gilding the lily, counsel refrained from summoning a myriad of witnesses to corroborate the uncontradicted testimony of the Commissioner's witnesses which the Tax Court had so ably summarized the day before. Counsel also refrained from introducing the appointment books from the Camden office which showed that four patients were scheduled per hour.

The Tax Court did an about face in its opinion which was handed down 19 months after the witnesses had testified (R 2a). It completely rejected the witnesses' testimony and reversed its trial position by stating (R 147a):

"This testimony was given years later when memory had dimmed and we are not convinced that the estimates were accurate."

The Tax Court's action at the trial put the issue on the length of the average visit at rest. Counsel were fully justified in relying upon the Court's remarks and in concluding that further substantiating proof was not required. See *Benner v. Atlantic Dredging Co.*, 134 N. Y. 156, 31 N. E. 328 (Ct. of Appeals, N. Y. 1892), citing *Flora v. Carbean*, 38 N. Y. 111 (1868).

There is absolutely nothing in the record to support the Tax Court's arbitrary rejection of this competent, relevant, credible and uncontradicted testimony. Taxpayers have not been given a fair hearing. Taxpayers do not owe any tax to the Commissioner and the testimony of the available patients can conclusively establish this.

C. Arbitrary Denial of Opportunity to Establish the Truth of the Matter.

The Tax Court recognizes that if counsel is reasonably warranted in concluding that a particular fact is not in controversy, with the sitting judge making a contrary determination, the taxpayer then is *entitled*, as a matter of law, to a rehearing by the Tax Court in order to adduce evidence pertaining to that fact. See *Mae F. Meurer*, 20 TC 614 (1953).

Taxpayers' counsel timely filed a motion with the Tax Court to grant a new hearing (R 161a-162a) so that taxpayers could produce additional witnesses to establish the length of time that the patients spent with taxpayer on an average visit. *Taxpayers even suggested in the motion that the Tax Court—not taxpayers—select the specific patients from a list of 5,000 patients who would then be called as witnesses and be questioned by the Tax Court to see, first, if their memories were accurate, and then to establish the length of the average visit with taxpayer.* This motion was summarily denied (R 2a).

The denial of this motion was arbitrary and unreasonable. Taxpayers have been deprived of their day in court because of this action.

Surely under these circumstances the Tax Court's refusal to permit the reopening of the case was an injustice and such a departure from the minimum requirements of fundamental fairness as to amount to a denial of due process. *Rochin v. California,* 342 U. S. 165, 172 (1952); *Duffin v. Lucas,* 55 F. 2d 786, 798 (CA 6, 1932). This is especially true where, as here, the opprobrious and punitive finding of fraud results because taxpayers failed to use proof which was available to them but unused because the Tax Court lulled them into a false sense of security.

D. Ignoring the Validity of the Patient Card Study.

The only issue in this case is whether taxpayer earned more income from his medical practice than he reported on his tax returns. Taxpayer knew that he had not and knew that it would be simple to prove that he had not.

Taxpayer engaged a certified public accountant to analyze his patients' medical cards to determine the number of visits made by each patient during each month during the period 1951-1955. (It will be recalled this period represents 80 per cent of the alleged unreported income.)

This detailed patient study, which gave the name and address of each patient (R 27a), was given to the Commissioner in 1958—five years prior to trial—with the request that the Commissioner interview these patients to verify the accuracy of the study (R 28a). Taxpayer also told the Commissioner he charged a set fee for each visit (R 46a-47a). This set fee was later stipulated to in open court (R 45b-46b). Taxpayer urged the Commissioner to multiply the set fee by the number of visits shown per patient and this would give a reconstruction of income that would fully support the tax return.

The Commissioner investigated the patient study and relied upon it for the selection of his own witnesses (R

120a). The Commissioner has never specified to the taxpayer any error in the study. The Commissioner did not call a single witness from the 5000 names who either stated that he visited the taxpayer more often than the study indicated or that he visited the taxpayer and paid him a fee which was not included in the study. It will be recalled that the Commissioner was contending—and had the burden of proving—that during this period, taxpayer was omitting annually some 11,473 visits on the average. *However, with 5000 names and five years of investigation, the Commissioner could not find one witness to support his contention.*

The Tax Court in its opinion simply ignored this facet of the case and the Third Circuit has held that this approach is free of error.

Holland states (at p. 135) that "leads reasonably susceptible of being checked, which, if true, would establish the taxpayer's innocence" may be considered as being true if the Commissioner fails to investigate. Here, the Commissioner did investigate (R 120a) but, apparently finding no error, ignores the situation and persuades the Tax Court and the Third Circuit to follow suit. This is clearly in violation with the principles espoused in *Holland* (at p. 135) that the Government's "duty is not to convict but to see that justice is done." This Court must exercise its power of supervision to correct this gross injustice.

E. Evidence Necessary to Sustain Fraud.

The Tax Court found the taxpayers guilty of fraud (including a year, 1948, when there was not a deficiency) solely on the grounds that they omitted substantial amounts of gross income (R 157a-158a). The deficiencies resulting from the "omitted" income were due to the fact that the taxpayers failed "to substantiate the acquisition prior to 1942 of a family cache of the size alleged" (R 155a). In essence, the Tax Court has held that a determination of a deficiency *ipso facto* establishes fraud, unless there is clear

and convincing proof by the taxpayer rebutting the deficiency. This is a clear error of law as Justice Stewart pointed out in his opinion in *Drieborg v. Commissioner*, 225 F. 2d 216 (CA 6, 1955), wherein he said (pp. 218-219):

> "At the outset it should be emphasized that the failure of the taxpayers to overcome the presumptive correctness of the deficiencies, even though those deficiencies cover a consecutive ten year period, cannot be regarded, in and of itself, as sufficient proof that the deficiencies or any part thereof were due to fraud on the part of the taxpayers. To hold otherwise would be to ignore the statute which imposes on the Commissioner the burden of proving fraud, and the often repeated admonition that such proof must be by clear and convincing evidence. *There must be additional independent evidence from which fraudulent intent on the part of the taxpayer can be properly inferred.*" (Emphasis added.) (Citations omitted.)

To the same effect see *Hawkins v. Commissioner*, 234 F. 2d 359, 360 (CA 6, 1956) where Justice Stewart sat on the panel.

These marked departures (subparagraphs A to E) from the accepted and usual course of judicial proceeding are tantamount to a denial of due process and call for an exercise of this Court's power of supervision.

CONCLUSION.

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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FRANK S. DEMING,
DAVID BERGER,
S. REGEN GINSBURG,
Attorneys for Petitioners.

APPENDIX "A".

Excerpt From Internal Revenue Code of 1939.

§ 1112. *Burden of Proof in Fraud Cases.*

In any proceeding involving the issue whether the petitioner has been guilty of fraud with intent to evade tax, the burden of proof in respect of such issue shall be upon the Commissioner.

Excerpt From Internal Revenue Code of 1954.

§ 7454. *Burden of Proof in Fraud and Transferee Cases.*

(a) *Fraud.* In any proceeding involving the issue whether the petitioner has been guilty of fraud with intent to evade tax, the burden of proof in respect of such issue shall be upon the Secretary or his delegate.

APPENDIX "B".

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT.

No. 15321.

WILLIAM S. AND MARY P. SERRI,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE

Argued November 18, 1965.
Decided December 2, 1965.
Rehearing Denied February 18, 1966.

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT OF THE UNITED STATES.

David Berger, Philadelphia, Pa. (Frank S. Deming, Philadelphia, Pa., on the brief), for petitioners.

Burton Berkley, Department of Justice, Tax Division, Washington, D. C. (John B. Jones, Jr., Acting Asst. Atty. Gen., Lee A. Jackson, John M. Brant, Jeanine Jacobs, Attorneys, Department of Justice, Washington, D. C., on the brief), for respondent.

Before KALODNER, *Chief Judge,* and MCLAUGHLIN and SMITH, *Circuit Judges.*

PER CURIAM:

On review of the record we find no error. The Decision of the Tax Court will be affirmed for the reasons so well stated in Judge Hoyt's Memorandum Findings of Fact and Opinion (T. C. Memo 1964-219).

APPENDIX "C".

CHART A

ALLEGED UNREPORTED INCOME

(R 142a-143a as modified by R 130a for 1950 and 1955)

1947		$ 3,820.79
1949		17,716.25
1950		14,804.85
1951	$49,310.13	
1952	24,530.43	
1953	30,779.26	
1954	38,398.34	
1955	51,945.92	194,964.08
1956		8,784.08
		$240,090.05

CHART B

MEDICAL INCOME PER 1040

(R 166a, 177a, 178a, 186a, 192a, 200a, 207a, 215a, 220a, 228a)

1947		$ 36,246.22
1949		41,990.19
1950		43,676.48
1951	$41,166.88	
1952	47,710.00	
1953	44,543.98	
1954	48,001.00	
1955	50,546.02	231,967.88
1956		54,382.29
		$408,263.06

CHART C

Year	*Medical Income Per 1040 (Chart B)*	*Stipulated Fee*	*Number of Patients to Produce Such Income*
1951	$ 41,166.88	$3.00	13.722
1952	47,710.00	3.00	15,903
1953	44,543.98	3.50	12,727
1954	48,001.00	3.50	13,715
1955	50,546.02	4.00	12,637
	$231,967.88		68,704
Average Annual Visits			13,741

CHART D

Year	*Alleged Unreported Income (Chart A)*	*Stipulated Fee*	*Number of Patient Visits to Produce Such Income*
1951	$ 49,310.13	$3.00	16,437
1952	24,530.43	3.00	8,177
1953	30,779.26	3.50	8,794
1954	38,398.34	3.50	10,971
1955	51,945.92	4.00	12,986
	$194,964.08		57,365
Average Additional Annual Visits			11,473

CHART E

	Rule 50 Computation of Unreported Income ($194,964.08) (Chart A) Plus the Gross Medical Income Reported on Taxpayers' 1040 ($231,967.88) (Chart C)	*Tax Court Computation on 7 Patients for 13 Hour Day for 275 Days at Stipulated Fees*
1951	$ 90,477.01	$ 75,075.00
1952	72,240.43	75,075.00
1953	75,323.24	87,587.50
1954	86,399.34	87,587.50
1955	102,491.94	100,100.00
	$426,931.96	$425,425.00

CHART F

	Medical Income Reported on 1040 as Filed (R 192a, 200a, 207a, 215a, 220a) (Chart C)	*Commissioner's Witnesses' Testimony of Four Patients an Hour for 13 Hours a Day for 275 Days at Stipulated Fee*
1951	$ 41,166.88	$ 42,900.00
1952	47,710.00	42,900.00
1953	44,543.98	50,050.00
1954	48,001.00	50,050.00
1955	50,546.02	57,200.00
	$231,967.88	$243,100.00

EXCERPTS FROM STIPULATION OF FACTS.

It is hereby stipulated that, for the purpose of this case, the following statements may be accepted as facts, subject to the right of either party to object to the admission of such facts in evidence on the grounds of materiality and relevancy; provided, however, that either party may introduce other and further evidence not inconsistent with the facts herein stipulated.

It is further stipulated that all exhibits referred to herein and attached hereto are incorporated in this stipulation and made a part hereof.

* * *

17. * * *

Respondent has not alleged that petitioners had any concealed source of income or that their income is derived from any illegal activity.

* * *